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C O N T E N T S

Economic Indicators

The United States

Recently released economic data show that the economy continues to grow at a healthy pace and that inflation shows no signs of reigniting. Interest rates, however, are substantially above their levels of a year ago and could cause economic growth to slow considerably if they rise much further.

The unemployment rate fell from 7.8 percent in April to 7.4 percent in May, the first monthly decline since January. The unemployment rate is now at the same level that it was in January 1981 when President Reagan took office.

Industrial production rose 1.4 percent in April, its seventeenth consecutive monthly increase and sharpest rise since January of this year. Industrial production is now 6 percent above the previous peak reached in July 1981.

The index of leading economic indicators rose a modest 0.5 percent in April. The index fell 0.1 percent in March after having risen for 18 consecutive months. The slowdown in the growth rate of the index suggests that the economic expansion will probably slowdown by the end of the year.

Consumer prices rose 0.5 percent in April, up from the 0.2-percent increase in March. Since the beginning of 1984, consumer prices have increased at a 5.1-percent annual rate.

After rising 0.5 percent in March and 0.4 percent in February, producer prices were unchanged in April. A sharp decline in food prices offset an increase in gasoline prices. Since January, producer prices have increased at a 4.6-percent annual rate.

Long-term interest rates rose in May, while short-term rates fell. The yield on 30-year Treasury bonds rose from 13.25 percent to 13.5 percent; in May 1983 the yield was 10.25 percent. The yield on 3-month Treasury bills fell from 10.0 percent to 9.75 percent; in May 1983 the yield was 8.0 percent.

On foreign exchange markets the dollar was slightly weaker against most of the major European currencies and slightly stronger against the Canadian dollar and the Japanese yen.

The merchandise trade deficit reached a record $12.2 billion in April, the fourth consecutive monthly record. For the first 4 months of 1984, the deficit was $42.0 billion, nearly triple the deficit in the same period last year.

International comparisons

The London economic summit of the seven largest industrial democracies ended on June 9 with renewed commitments to the liberalization of international trade. Third world debt, energy supplies, and East-West relations were the summit's major concerns.

Growth in the OECD area continues, but labor strife in Great Britain and the Federal Republic of Germany is beginning to have a noticeable effect on economic performance.

Industrial production.--According to the Chemical Bank, the growth of industrial output in almost all major industrial countries showed a pronounced slowdown in March and April. Seasonally adjusted industrial output declined at a 0.4 percent annual rate in the United Kingdom during the first quarter of 1984 (see statistical tables). The U.K.'s industrial production fell by 1.5 percent in March, according to Britain's Central Statistics Office. The coal miners' strike, slashing coal production by 45 percent, had a major role in the March decline. The growth in Japanese industrial output was 13.6 percent during the first quarter of 1984 (see statistical tables).

Employment.--CIA data show that West Germany's seasonally adjusted unemployment rate climbed to 9.3 percent in April from 8.8 percent during the first quarter of 1984. Strikes, lock-outs, and lay-offs in connection with West German metalworkers' demand for the 35-hour work week may have idled 180,000 workers in the Federal Republic during the second half of May. The labor strife disrupted West Germany's automobile industry and has generated pessimistic assessments about the country's 1984 and 1985 growth prospects. Without taking the effect of the labor problem into account, the growth of West Germany's GNP is expected to be 3 percent in 1984 and less than that in 1985.

For the month of April, the CIA reported seasonally adjusted unemployment rates of 9.5 percent for France, 12.6 percent for the United Kingdom, and 11.4 percent for Canada. In all these countries, the unemployment rate was higher in April than during the first quarter of 1984. Japan's unemployment rate was 2.7 percent in January-March 1984.

External balances.--The International Monetary Fund (IMF) reported that Japan had a $3.8-billion surplus in its April 1984 merchandise trade balance. This exceeded by $1.2 billion Japan's merchandise trade surplus during the corresponding period of 1983. Japan's surplus in its current account was $4.9 billion during the first quarter of 1984, according to the CIA. Tokyo agreed to take steps to internationalize the yen in order to increase foreign demand for it. (See separate article on the Japanese announcement in this issue's international trade developments section.) The resulting appreciation of the Japanese currency is expected to reduce the country's exports while increasing its imports.

The Chemical Bank reported that West Germany's merchandise trade surplus narrowed in April to $1.0 billion from $1.7 billion in March. West Germany's first quarter 1984 current account surplus was $0.8 billion, according to the CIA. Quoting news agencies, the IMF reported that France's merchandise trade deficit of $270.1 million in March worsened to $522.4 million in April.

According to Britain's Department of Trade and Industry, the United Kingdom suffered a record current account deficit of $821 million during the month of April. Deterioration in the country's oil trade surplus may have been the major factor in this largest-ever current account deficit. During the first quarter of 1984, the U.K. had a current account surplus of $1.1 billion, according to the CIA.

Figures released by the Bank of Italy showed a $722-million surplus in the country's balance of payments in April 1984. However, Italy's balance of payments indicated a deficit of $1.2 billion during the first four months of 1984. The improvement is attributed to the start of Italy's tourist season.

Prices.--The British Government reported that the country's inflation was 5.2 percent in April. Compared with the last quarter of 1983, Britain's consumer prices rose at a seasonally adjusted 4.3 percent during the first quarter of 1984 (see statistical tables). Japan's seasonally adjusted consumer prices increased by 3.6 percent in January-March 1984 (see statistical tables). Statistics Canada reported that Canadian consumer prices increased at a seasonally adjusted 0.5 percent from March to April.

Forecasts.--According to Sweden's Handelsbanken, the four Nordic nations (Finland, Denmark, Norway and Sweden) are leading Western Europe in the current economic recovery, with Finland leading the Nordic nations. Finland's 1984 GNP is estimated to be growing at an annual rate of 5.0 percent, and the four nations' combined growth rate is an estimated 3.5 percent. The Banco de Espana, Spain's central bank, forecasts that Spain's GNP will grow by 2.5 percent in 1984. Growth prospects in the Benelux countries are weaker. Data Resources Europe, Inc. estimates that the GNP of the Netherlands will grow at a 1.9 percent rate in 1984, and that of Belgium, just over 1 percent.

Although IMF sees some moderation in the growth of industrial countries later this year, it predicts a continued brisk recovery in 1985. The independent London-based National Institute of Economic and Social Research says that, although some acceleration in OECD consumer prices may take place in the near future, inflation in the OECD area will remain between 5 percent and 6 percent in both 1984 and 1985. The Institute predicts that the volume of world trade will grow by 5.5 percent both this year and in 1985. The General Agreement on Tariffs and Trade (GATT) predicts growth in the volume of world trade of approximately 4 percent in 1984.

International Trade Developments

A new trade round waits offstage

Calls for a new round of multilateral trade negotiations have surfaced with increasing frequency in recent months in statements of government officials and other trade observers. A chorus of spokespersons for the U.S. and Japanese governments have promoted the idea. During a recent series of trade hearings held by Senator Roth's Joint Economic Subcommittee on Trade, Productivity, and Economic Growth, witnesses from academia, U.S. government agencies, and the private sector alike underscored the urgency of elevating trade concerns out of the routine of day-to-day squabbles and onto the grand scale of multilateral negotiations. Nevertheless, disagreement among governments on the timing for such negotiations has held up transforming pronouncements into a solid commitment.

The reasons for this disagreement are several. First, the European Community is wary of starting a round before economic recovery has taken firm hold there. EC Commission Vice President Wilhelm Haferkamp has also stressed that thorough preparations and the establishment of clear objectives must precede entrance into new negotiations. This statement reflects European concern that the United Stated is in too much of a hurry to announce the start of a new round. Second, U.S. trading partners are worried about the trade implications of the U.S. budget deficit on worldwide interest rates and growth, a perceived rise in U.S. protectionism, and election-year politics. Finally, some GATT members assert that the results of the ambitious work program undertaken at the 1982 GATT Ministerial should be assessed before a trade round is formally initiated.

Most major trading partners agree on the agenda of trade problems that the proposed round should address. Negotiations would tackle a wide range of issues including conclusion of safeguards and counterfeiting codes, trade in services, subsidies (especially agricultural subsidies), structural adjustment, the operation of GATT dispute-settlement mechanisms, and North/South trade. The United States also wants talks on high-technology trade, but has not yet defined to other countries' satisfaction what the goals of such talks would be. The 1982 GATT Ministerial work program was aimed at stimulating discussion and data collection work on most of these topics.

Unfortunately, there is not yet a consensus on how to solve these problems through multilateral action. Clearly, the success of any major trade negotiation hinges on brokerage among the interests of the United States, the European Community, and the developing countries. Progress toward an agreement on the linked issues of safeguards and structural adjustment has been stalled by the differing priorities of developed and developing countries. Moreover, the United States and the European Community continue to disagree on goals and priorities in several key areas. The U.S. emphasis on the need to liberalize trade in services and high-technology goods illustrates this point. The European Community places barriers to trade in services much lower on its list of complaints than does the United States. Neither does the European Community receive graciously the United States' still-vague high-technology trade proposals when the Community is struggling to protect its own troubled high-technology industry.

The United States and Japan are convinced that the very fact of starting a new round of negotiations would help stem protectionism and narrow differences in policy. However, the Europeans and the developing countries fear that the current intensity of protectionism and the wide gaps in the parties' positions on vital issues may result in a failure of negotiations. They point out that trade declarations of the economic summit group, the OECD, and the GATT to "roll back" protectionist measures have yielded no concrete results as yet and that observance of these commitments would inspire confidence in the ability of a new round to reduce trade barriers.

Serious commitments to negotiate are now likely to await the year-end GATT meetings that will assess progress on the Ministerial work program. With the U.S. presidential elections over by that time, campaign-inspired demands for U.S. domestic protection should subside somewhat. Setting a date for negotiations even after yearend will depend on improved economic conditions in Europe. At the London economic summit, the United States and Japan moderated their stance somewhat by calling for the start of negotiations in 1986, with preparations during 1985. In a recent speech to the European Atlantic Group in London, GATT Director-General Arthur Dunkel warned that "to reach the stage of negotiation requires that we survive the stresses of the next few months without serious conflict, and that the ground be prepared with the greatest possible care."

Commerce Rules Out Countervailing Duties for NME's

In determinations published on May 7, the Commerce Department ruled that subsidies within the meaning of section 303 of the Tariff Act of 1930 cannot be found in nonmarket economy countries (NME's). The determinations resolved an ambiguity in U.S. countervailing duty (CVD) law. Since section 303 refers to bounties or grants by any political entity, it was potentially applicable to NME's. But most experts believed that identifying, much less measuring, a subsidy in an NME would be difficult or impossible. The issue was mainly of theoretical interest until 1983, when the first petition alleging subsidization by an NME was filed. This petition, which involved textile imports from China, was followed by petitions against imports of carbon steel wire rod from Czechoslovakia and Poland (1983), and potassium chloride from East Germany and the Soviet Union (1984). Because the Chinese textiles petition was withdrawn before Commerce could issue a ruling in the investigation, the application of countervailing duty law to NME's was not tested until the investigations on carbon steel wire rod.

Petitioners argued that the governments of Czechoslovakia and Poland subsidize producers or exporters of steel wire rod through a variety of measures, including multiple exchange rate systems, tax exemptions, and currency retention programs that allow enterprises to retain some of their earnings from hard-currency exports. Since these countries have not acceded to the GATT Subsidies Code, they are not entitled to an injury test under title VII of the Tariff Act. (For duty-free items, the two countries are entitled to an injury test under section 303(b) because they are GATT signatories.)

Based on a literal reading of section 303, Commerce preliminarily determined on February 16, 1984, that Congress had not exempted NME's from CVD law. At the same time, it did not find any reason to believe that benefits constituting bounties or grants as defined in section 303 were being conferred on Czech or Polish producers. In its final determination Commerce concluded that Congress did not intend section 303 to be applied to NME's; that bounties or grants within the meaning of CVD law cannot be found in NME's; and that Czechoslovakia and Poland are NME's.

The two determinations, which are virtually identical, defined a subsidy as "any action that distorts or subverts the market process and results in a misallocation of resources, encouraging inefficient production and lessening world wealth." Commerce argued that it is meaningless to apply a concept based on distortions of the market to NME's where resources are allocated not by the market but by planners. Commerce identifies a subsidy in a market economy by comparing the treatment a firm would receive in the marketplace with the special treatment it receives from the government. In the case of an NME, Commerce argued, it is impossible to disaggregate government actions to isolate the exceptional one that is the subsidy. To do this, the department would have to consider every NME government action a subsidy (or a tax if it harmed the enterprise). According to this argument, the essential distinction between market economies and NME's revolves around prices and profits. In an NME prices are administered and do not reflect scarcities. Similarly, profits may be viewed as administered since prices for the enterprise's inputs and output are set. Profits drive market economies, but in an NME they may be only one among several success indicators established by the government to influence enterprise behavior. Addressing the petitioners' allegations directly, Commerce concluded that the alleged subsidies are "elements of control" rather than incentives.

Not finding any evidence that Congress ever directly addressed the issue of countervailing duties and NME's, the Commerce Department attempted to figure out what Congress would have said. It concluded that there is no indication that Congress meant the CVD law to be applied to NME's.

Absent a challenge to Commerce's rulings in CVD cases, domestic producers seeking relief from imports from NME's will be forced to rely on the antidumping provision of title VII of the Tariff Act of 1930 and the market disruption provision of section 406 of the Trade Act of 1974.

U.S. firms asks action against foreign subsidies on satellite launching services

Initiating the first request for relief from subsidized imports of a service, Transpace Carriers, Inc., a private U.S. satellite launching service, filed an unfair trade practices complaint with the Office of the United States Trade Representative (USTR). In a petition filed on May 25, Transpace alleges that its French competitor, Arianespace, S.A., is being subsidized by the French Government and is selling its satellite launching services at unfairly low prices in the U.S. market. The Transpace petition seeks Presidential action under section 301 of the Trade Act of 1974.

Section 301 is a catchall provision, under which the President is directed to take "all appropriate and feasible action within his power to . . . obtain the elimination of . . . any act, policy or practice of a foreign government or instrumentality that . . . is unjustifiable, unreasonable, or discriminatory and burdens or restricts United States commerce." Using section 301 is not generally the first choice of firms seeking trade relief, since the remedy it provides is not specified by law and the President has wide discretion as to whether and how to pursue a 301 case. However, since the more commonly-used unfair import procedures--the dumping, countervailing, and unfair practices (sec. 337) laws--apply only to unfair imports of tangible goods, there was no choice in this case.

Transpace was formed in 1982 with the purpose of launching the Delta series of rocket boosters originally developed by the National Aeronautics and Space Administration (NASA). In the Reagan Administration's efforts to encourage private sector firms to tap the commercial potential of the space industry, NASA's Delta program was terminated, and Transpace was allowed to purchase the Delta program from NASA and commence private sector commercial launch operations. A new entrant in the fledgling commercial space industry, Transpace has yet to perform any commercial launches. To date, the firm has lost two bids, one to Arianespace and the other to the U.S. Government, in the form of NASA's Space Shuttle program. Transpace contends that the market for worldwide space transportation through 1990 is worth more than $10 billion, and that it is an infant industry requiring protection from unfair competition to succeed.

On May 22, Transpace's French competitor fired its first launch, putting into orbit a GTE Spacenet communications satellite. Although European satellite launching capability was originally developed by the eleven member governments of the European Space Agency (ESA), with the French national space agency as the prime contractor, Arianespace was created as a private firm in 1980 to provide commercial launching of the ESA-developed Ariane vehicles. Since the transfer of the Ariane program from the public to the private sector, however, Transpace alleges that the French firm has been receiving subsidies from ESA member states.

In particular, Transpace cites five specific subsidy practices of the ESA, and requests Presidential action in each of these areas. First, the firm requests the President to seek immediate discontinuance of Arianespace's two-tiered pricing policy. Currently, the French firm charges the eleven members of the ESA 25 percent more for rocket launch services than is charged to non-ESA members; one-half of Arianespace launches are conducted for ESA countries.

Second, Transpace seeks the elimination of cost-free or below-cost support of launch facilities, services, and personnel provided to Arianespace by the French national space agency, the Centre National d'Etudes Spatiale. Third, Transpace wants to end government subsidies of launch mission insurance rates, charges which customers of the French company would otherwise pay. Fourth, Transpace requests that all outstanding and future Arianespace bids to provide launch services reflect the firm's actual costs, plus a reasonable profit per launch.

Finally, if the French firm does not act to eliminate the described unfair trade practices, Transpace requests the President to retaliate by prohibiting Arianespace from advertising and marketing its services in the United States, and more importantly, by imposing economic sanctions against goods and services of the eleven ESA member states.

Are foreign partners preferable to foreign creditors?

Some Latin American countries have recently begun to show a greater interest in attracting foreign investment. With foreign commercial credit severely curtailed since the eruption of their debt crises, these countries now eye foreign investment as a possible alternative for financing their economic revitalization.

The U.S. Government has long recommended that debt-ridden developing countries welcome foreign investors as a means of easing their capital shortage. Restrictions by Mexico and Brazil to the free flow of investment--such as limiting foreign participation in new ventures, restrictive investment performance requirements, tax measures, and control of remittances to foreign countries--have been a frequent subject of bilateral consultations between the United States and both countries.

Mexico.--In February, Mr. Hector Hernandez, Mexico's Minister of Commerce and Industry, made public a list of 34 industries where foreign owners or partners are now welcome. (Mexico announced earlier that it would allow majority participation of foreign investors up to 100 percent.) In releasing the list, along with new investment regulations containing various provisions aimed at attracting foreign entrepreneurs, Mr. Hernandez stated that "direct foreign investment is a viable option which can help us to achieve our national goals." The industries on the list include farm machinery, wood-working equipment, petrochemical hardware, machine tools, electric generators, turbines, and turbocompressors. Significantly, high-technology industries such as telecommunications equipment, computer components, precision medical instruments, and photographic equipment are also specified.

Mexico, one of the noncommunist world's most closed economies, has been following a restrictive foreign investment policy for a long time. As a result, direct foreign investment is estimated to account for only 4 to 5 percent of Mexico's overall gross fixed investment. U.S. investors account for 68 percent of this total compared with 75 percent a decade ago. Mexico's 1973 foreign investment code has limited foreign entrepreneurs to minority ownership and excludes or severely restricts foreign participation in certain "strategic" industries such as telecommunications and the petroleum industry, including petrochemical products.

Immediately after taking office in December 1982, President de la Madrid signaled a shift in this policy. The Mexican President expressed interest in the benefits of direct foreign investment like job creation, the transfer of technology, and export-marketing experience. Nonetheless, he did not set out to change the restrictive 1973 law. Insisting that new legislation was not needed, the de la Madrid Government announced that it will instead apply the 1973 statute in a "flexible" manner. New regulations on foreign investment were issued in February to implement this policy of flexibility.

Moreover, the Mexican Government reportedly will allow foreign investors to bid for the shares of 339 government-owned companies it plans to auction off. The previous Administration had acquired these shares from Mexican commercial banks when it nationalized the banks in 1982. The sale of the shares to private bidders--domestic and foreign--is expected to reduce the role of the public sector in the Mexican economy, which increased significantly as a result of the 1982 nationalizations. However, the current administration plans to retain control of 128 other private companies seized in the 1982 takeover of the banks.

"Partners are preferable to creditors" is a stance advocated strongly in some Mexican business circles. Still, considerable opposition to foreign investment persists in all segments of Mexican society, including some other quarters of private business. Voices critical of a changed investment policy insist that foreign capital has proved detrimental to Mexico's economic development in the past. All considered, the future of direct foreign investment in Mexico is uncertain.

Brazil.--Among many ideas on how to resolve Brazil's debt crisis and raise new capital, the concept of "debt-for-equity" is reportedly gaining popularity. Proposals are circulating to convert part of Brazil's foreign debt into equity now held in either privately-owned or state-owned companies. (The borrowing of state-owned companies is believed to represent about two-thirds of Brazil's international debt.)

In historical perspective, the Brazilian climate has been more hospitable to foreign ventures than the Mexican. Nonetheless, Brazilian law favors foreign loans over direct foreign investment; for example, it puts fewer obstacles in the way of interest remittances than profit remittances. As in Mexico, regulations in Brazil exclude foreign investment in specified areas considered critical for economic development. In Brazil, these include petroleum exploration and refining, telecommunications, and many areas of the computer industry.

Like their Mexican counterparts, Brazilian authorities now insist that no new legislation is needed to spur foreign investment. They claim, for example, that debt can be converted into direct investment under existing law. Creditor banks have the option of selling their Brazilian paper to multinational companies with subsidiaries in Brazil. These, in turn, are free to convert their new obligations into equity, register it as direct investment with the Central Bank of Brazil (which controls all transactions involving foreign exchange), and reap the attendant tax benefits of direct investment.

Liberalization of Japan's financial markets announced

On May 29, U.S. Secretary of the Treasury Regan and Japanese Minister of Finance Takeshita agreed to adopt the recommendations of a working group formed to study ways to liberalize Japan's financial markets. The report suggests steps that should be taken by the Japanese Government to allow greater use of yen-based financial instruments by encouraging the creation of a world-wide Euroyen market and by allowing foreign companies greater access to Japan's capital markets. These moves are widely expected to accelerate deregulation of Japan's domestic financial markets, ultimately making Japanese interest rates more responsive to global credit demands.

The United States has urged Japan to relax restrictions on foreign participation in its financial and capital markets, both to take pressure off the dollar in foreign exchange markets and to allow the international financial system to operate more efficiently. As recently as 1978, Japan still retained formidable barriers to both inflow and outflow of capital. The Foreign Exchange Control Law that took effect at the end of 1980 made it easier for foreigners to hold Japanese securities. Short-term capital flows were almost completely liberalized, but foreign access to long-term financial instruments remained tightly controlled and foreign-affiliated banks in Japan continued to operate under numerous restrictions.

In the May 29 package, the Japanese Government agreed to relax controls on Euroyen loans and bonds, thus allowing more dealing in yen outside Japan (The Economist, May 26, 1984). It also agreed to eliminate some of its restrictions on the operations of foreign banks in Japan. For example, all firms engaged in underwriting securities, in or out of Japan, will now be able to participate in the Euroyen bond market. Quota restrictions on international lending of yen by Japanese banks were also removed, and foreign banks will be allowed to engage in trust banking and pension fund management starting on December 1, 1984.

By the end of 1984, U.S. and other foreign banks will be permitted to issue short-term Euroyen certificates of deposit (CD's) from their offices outside Japan. As of April 1985, the minimum denomination of certificates of deposit (CD's) issued in the Japanese market will be lowered and the total amounts that each bank can issue will be raised. CD's are not subject to interest rate ceilings.

Though billed by the U.S. Treasury Department as an exchange rate package, the effects of the liberalization measures on Japan's domestic financial market, on U.S.-Japanese trade, and on the yen-dollar exchange rate are now being hotly debated. One argument, exemplified by a Business Week article on June 11, is that the measures are "unlikely in the near term to do what they were meant to do: strengthen the yen and substantially alter U.S.-Japanese trade patterns."

According to this view, a liberalization could produce a net outflow of capital from Japan because the lower long-term interest rates now prevailing in Japan would spur U.S. borrowers to raise funds in Japan rather than domestically. Many U.S. firms will convert those funds into dollars, thus bidding up the dollar's exchange rate. Increased demand for funds in Japan will tend to offset this effect by bidding up Japanese interest rates, causing the yen to appreciate. However, the Japanese Government could easily offset this pressure by increasing the money supply to accommodate these new demands.

Other analysts suggest that as a result of the measures, Japan's financial market will be more open to market influences, particularly by foreign participants (JEI Report, No. 22B, June 8, 1984). The number of yen-denominated asset instruments available to both foreign and Japanese firms will be raised as a result of the package, as will the availability of instruments whose interest rates are market-determined. At the same time, pressures within Japan to liberalize interest rates are likely to be mounting for another reason: the first large issue of government bonds, which was sold in 1975, will be coming due in 1985. The Government is likely to face demands from Japanese and now foreign banks for higher interest rates on those bonds.

The new liberalization measures will allow market forces--both domestic and international--to have greater play in Japan's capital markets, a development in the interest of both Japan and the United States. They have also created the basis for the yen's appreciation, but any appreciation in itself will create an offsetting downward force on the value of the currency: the advantage to a foreign borrower of lower Japanese interest rates may easily be eliminated if they must repay their debts in higher-priced yen.

U.S. offensive against export credit war

In October 1983, the United States and other member countries of the OECD's International Arrangement on Export Credits achieved agreement to peg export finance lending rates to market rates. As a result, the offering of official loans at interest rates lower than the minimum guidelines established under the Arrangement was virtually eliminated as a means of winning export contracts. Predatory financing has taken a new form, however, with a number of countries combining direct aid assistance with conventional loans in mixed credit packages. France has been the leader in this export credit war, but countries such as Japan, Canada, and the United Kingdom are regularly using blended credits. The United States has also joined the battle, offering similar credit terms in an effort to curb the practice. In addition, U.S. officials are trying to negotiate a higher minimum for the grant portion of a credit package, a change in the international export guidelines that they hope will make it too expensive for countries to subsidize exports under the guise of aid.

The U.S. role in the competition has been limited to two preliminary loan commitments that, strictly speaking, are not mixed credits since they contain no direct grant components. Early in March, the U.S. Export-Import Bank (Eximbank) announced a heavily subsidized loan arrangement to enable Cincinnati Milicron, a machine tool manufacturer, to meet a mixed credit package that France had offered an Indonesian aircraft manufacturer. The Eximbank financing, which covers 100 percent of some $10 million to

$15 million in potential U.S. exports, provides for a 33-year repayment period (rather than the normal 5- to 10-year period) at only 6.5 percent interest. The actual repayment terms offered are 20 years following a 13-year grace period. Less than 2 weeks later, Eximbank announced another highly concessional financing package to again match a French mixed credit offer. This second Eximbank offer was made to enable Stromberg-Carlson, a Florida-based firm, to compete for an estimated $25 million sale of digital switching equipment to the Cyprus Telecommunications Authority, the Government-owned national telephone utility. The terms of the loan again provided for 100-percent coverage of the potential U.S. export transaction, rather than the normal Eximbank coverage of 65 percent, an interest rate of 7.62 percent, and a repayment period of 20 years after a 10-year grace period. Eximbank officials stated that both actions were taken to counter predatory financing by France and to discourage such future action by foreign governments. Before this credit war is over, however, repeated battles could become expensive (e.g., Eximbank's bid for the sale of machine tools to Indonesia was recently accepted and has been authorized by the bank). The United States would therefore prefer the route of negotiation.

For the past several months, U.S. officials have been trying to negotiate a higher minimum level for the direct aid component of mixed credit financing. At present, the International Arrangement on Export Credits permits a grant, or so-called development funds, to be included as part of a credit package, but requires that the minimum level of aid that can be offered is 20 percent. It also requires that exporting countries offering mixed credit packages with aid elements below 25 percent notify the OECD 10 days in advance to give competitors a chance to match the bids. The reason for requiring notification is that any mixed credit offering with less than a 25-percent aid component has traditionally been considered to be a subsidized loan, whereas any offering exceeding the 25-percent threshold has been considered a genuine attempt to provide development funds to the importing country. Recently, however, many mixed credits have contained an aid component of just over 25 percent. Thus, although the United States would prefer that the aid element of official export financing be eliminated, it is now attempting a partial solution by seeking a consensus among the creditor countries to raise the minimum threshold for aid to 50 percent.

This U.S. proposal was considered at a series of talks on the International Arrangement on Export Credits held in April and at the OECD ministerial meeting held in May. Although not accepted, a higher aid minimum has not been rejected. Department of Treasury officials will be holding bilateral talks on the issue during the summer, and further multilateral talks will again be held in September.

Can Korean shipbuilders chart a new course?

Ignoring a world-wide shipbuilding recession that halved the tonnage produced between 1976 and 1977, Korea captured enough orders to become the world's second largest shipbuilder, following Japan. After entering the international market in the mid-1970's, Korean shipbuilders successfully diversified their market by building different and advanced types of vessels and offshore oil platforms and equipment. The nation also moved successfully into shipbuilding's secondary industry, ship repair. Today the shipbuilding and ship repair industry is one of Korea's largest sources of foreign exchange earnings.

A key element in Korea's shipbuilding growth has been the subsidized co-financing program of the Korean Export-Import Bank (KEXIM). By providing low-cost financing to Korean shipyards and long-term, low-cost financing to purchasers, KEXIM assistance helped woo customers from Europe and Japan and contributed to Korea's success in capturing a major portion of the market.

But now Korea's shipbuilders are struggling to maintain their share of the market. A worldwide decline in demand for new vessels and increased foreign competition has resulted in fewer orders for Korean yards. In the first quarter of 1984, only 22 new orders were won by Korea's leading shipyards--Hyundai, Daewoo, Sansung, and KSEC. With a backlog of export orders for 189 vessels worth $3.5 billion, these shipyards have enough work to keep them busy in the short term. The Koreans are concerned, however, that orders are not being replaced fast enough to keep the yards busy beyond mid-1985 when production of the present backlog of orders is completed. Without more new orders, Hyundai will start to have gaps in its delivery schedules after July 1985 and Daewoo, in a slightly better position, will have gaps in delivery after late 1986 or 1987.

Policy changes currently being considered by KEXIM to maximize the effectiveness of its resources could place additional pressures on Korea's ability to maintain its market share. KEXIM is considering increasing its interest rate for all loans under co-financing from 9 percent to 10 percent. This would result in increased pre- and post-delivery costs for shipbuilders. KEXIM is also considering decreasing its portion of co-financing transactions from 56 percent to 50 percent, thereby requiring greater participation by commercial banks and contributing to higher costs. Finally, the bank is now considering directing more of its resources to other export industries and reducing its assistance to the shipbuilding industry. Until now, about 85 percent or more of KEXIM loans have gone to shipbuilding. This could result in fewer approvals for shipbuilding co-financing deals and mean fewer sales and decreased revenues for the shipyards.

Industrial production
(Percentage change from previous period, seasonally adjusted at annual rate)

Country	1981	1982	1983	1983 I	1983 II	1983 III	1983 IV	1984 I	1983 Dec.	1984 Jan.	1984 Feb.	1984 March	1984 April	1984 May
United States	2.6	-8.1	6.4	9.9	18.4	21.8	10.1	11.6	6.4	19.2	12.8	6.2	17.7	5.0
Canada	0.9	-10.7	5.9	22.1	13.1	18.5	13.8	3.6	13.0	31.8	-33.5	1.8		
Japan	1.0	0.4	3.5	3.6	6.5	14.0	10.3	13.6	6.8	4.4	48.5	-14.7	23.5	
West Germany	-2.3	-3.2	0.4	4.4	6.0	4.9	9.0		-9.3	12.9	6.2			
United Kingdom	-3.9	2.0	2.9	5.3	0.5	5.7	3.3	-0.4	13.8	4.7	-18.8	-15.2		
France	-2.6	-1.5	1.2	1.0	4.2	3.1	1.0	5.2	-8.7	9.6	-16.7	31.5		
Italy	-2.4	-2.2	-4.8	-2.0	-10.4	-4.9	17.6		-42.2					

Source: Economic and Energy Indicators, U.S. Central Intelligence Agency, June 8, 1984.

Consumer prices
(Percentage change from previous period, seasonally adjusted at annual rate)

Country	1981	1982	1983	1983 I	1983 II	1983 III	1983 IV	1984 I	1983 Dec.	1984 Jan.	1984 Feb.	1984 March	1984 April	1984 May
United States	10.3	6.2	3.2	-0.4	4.3	4.2	4.4	5.0	3.2	7.8	4.4	2.8	5.6	
Canada	12.5	10.8	5.8	3.0	4.6	6.3	4.2	6.2	8.0	7.6	5.2			3.6
Japan	4.9	2.6	1.8	0.6	1.6	0.6	3.6	3.6	2.7	0.3	12.9	-0.2	-0.7	-0.8
West Germany	6.0	5.3	3.0	0.5	1.6	5.0	3.0	3.1	3.3	2.4	3.8	2.6	1.4	0.1
United Kingdom	11.9	8.6	4.6	3.6	2.2	8.2	6.1	4.3	6.4	2.1	6.4	2.3		
France	13.3	12.0	9.5	11.0	10.4	9.3	8.6	7.1	6.2	6.7	7.7	6.4	3.6	
Italy	19.3	16.4	14.9	13.4	14.4	12.5	11.1	11.2	10.1	11.8	11.1	11.4	10.9	7.3

Source: Economic and Energy Indicators, U.S. Central Intelligence Agency, June 8, 1984.

Unemployment rates
(Percent; seasonally adjusted; rates of foreign countries adjusted to be roughly comparable to U.S. rate)

Country	1981	1982	1983	1983 I	1983 II	1983 III	1983 IV	1984 I	1983 Dec.	1984 Jan.	1984 Feb.	1984 March	1984 April	1984 May
United States	7.6	9.7	9.6	10.4	10.1	9.4	8.5	7.9	8.2	8.0	7.8	7.8	7.8	7.4
Canada	7.6	11.0	11.9	12.5	12.2	11.6	11.2	11.3	11.1	11.2	11.3	11.4	11.4	
Japan	2.2	2.4	2.7	2.7	2.7	2.7	2.6	2.8	2.6	2.8	2.9	2.7		
West Germany	4.1	5.9	7.3	7.1	7.4	7.5	7.3	7.2	7.2	7.1	7.2	7.3	7.4	
United Kingdom	10.6	12.3	13.4	13.3	13.5	13.6	13.3	13.6	13.4	13.6	13.7	13.8	13.7	
France	7.7	8.7	8.8	8.7	8.8	8.8	9.0	9.5	9.2	9.3	9.6	9.7		
Italy	4.3	4.8	5.2	4.9	5.7	5.1	5.0							

Note.--Italian unemployment surveys are conducted only once a quarter, in the first month of the quarter.

Source: Statistics provided by Bureau of Labor Statistics, U.S. Department of Labor, June 1984.

Trade balances
(Billions of U.S. dollars, f.o.b. basis, seasonally adjusted at annual rate)

Country	1981	1982	1983	1983 I	1983 II	1983 III	1983 IV	1984 I	1983 Nov.	1983 Dec.	1984 Jan.	1984 Feb.	1984 March	1984 April
United States 1/	-27.5	-31.6	-57.4	-32.4	-54.8	-65.2	-77.6	-104.8	-75.6	-63.6	-99.6	-106.8	-108.0	-129.6
Canada	6.2	14.8	14.6	13.2	16.8	13.2	14.8	13.6	18.0	15.6	20.4	10.8	9.6	
Japan	20.1	18.4	31.6	27.6	31.6	33.2	34.8	40.0	39.6	34.8	39.6	39.6	40.8	44.4
West Germany	11.9	21.1	16.5	22.0	16.8	15.2	12.4	19.2	13.2	12.0	16.8	22.8	15.6	14.4
United Kingdom	6.4	3.6	-1.6	1.2	-4.0	2.4	0.8	-0.8	2.4	8.4	-6.0	7.2	-3.6	-14.4
France	-9.3	-14.0	-5.9	-14.0	-6.8	-1.6	-0.8	-6.0	-2.4	0	-7.2	-7.2	-3.6	-6.0
Italy	-15.9	-12.8	-7.9	-11.6	-5.6	-10.0	-3.2	-9.2	0	-4.8	-6.0	-4.8	-16.8	

1/ Exports, f.a.s. value; imports, customs value.

Source: Economic and Energy Indicators, U.S. Central Intelligence Agency, June 8, 1984.

U.S. trade balance, by major commodity categories and by selected countries
(Billions of U.S. dollars, customs value basis for imports, 1/ seasonally adjusted unless otherwise indicated)

Item	1981	1982	1983	1983 I	1983 II	1983 III	1983 IV	1984 I	1983 Nov.	1983 Dec.	1984 Jan.	1984 Feb.	1984 March	1984 April
Commodity categories:														
Agriculture	26.8	21.6	20.0	5.1	4.4	5.2	5.4	5.2	1.9	1.9	2.1	1.4	1.7	1.4
Petroleum and selected products, unadj	-73.0	-54.6	-49.1	-9.6	-11.3	-14.6	-13.2	-13.1	-4.3	-3.6	-4.3	-4.3	-4.5	-5.0
Manufactured goods	11.5	-4.9	-31.3	-4.1	-7.0	-7.9	-11.2	-19.0	-3.8	-4.0	-6.0	-6.3	-6.7	-7.2
Selected countries:														
Western Europe	13.5	7.6	1.2	2.0	-0.6	-0.1	0.2	-3.6	-.1	.2	-.7	-1.2	-1.7	-1.3
Canada	-6.9	-12.6	-12.1	-2.8	-4.1	-3.4	-3.7	-4.3	-1.1	-1.4	-1.5	-1.4	-1.4	-2.3
Japan	-15.8	-17.0	-19.6	-4.7	-4.3	-4.4	-6.2	-7.0	-2.1	-2.2	-2.4	-2.2	-2.4	-2.4
OPEC, unadj	-27.9	-8.3	-8.2	-.5	-1.1	-3.5	-3.1	-2.6	-1.0	-.5	-.9	-1.0	-.7	-1.4
Unit Value (per barrel) of U.S. imports of petroleum and selected products, unadj	$34.28	$31.48	$28.60	$29.77	$27.79	$28.49	$28.43	$28.31	$28.34	$28.19	$27.98	$28.46	$28.49	$28.48

1/ Effective January 1982, the Census Bureau replaced f.a.s. value with customs value in various reports on the U.S. trade balance. Data presented in this table for January 1982 and thereafter reflect the customs value for imports. Data presented for December 1981 and before reflect the f.a.s. value.

Source: Summary of U.S. Export and Import Merchandise Trade, U.S. Dept. of Commerce, April 1984.

Money-market interest rates
(Percent, annual rate)

Country	1981	1982	1983	1983 I	1983 II	1983 III	1983 IV	1984 I	1983 Dec.	1984 Jan.	1984 Feb.	1984 March	1984 April	1984 May
United States	15.9	12.4	9.1	8.5	8.8	9.6	9.4	9.7	9.7	9.4	9.6	10.1	10.4	11.1
Canada	18.4	14.4	9.5	9.8	9.4	9.4	9.5	10.0	9.8	9.8	9.9	10.4	10.8	11.5
Japan	7.5	6.8	6.8	6.6	6.5	6.6	7.6	6.4	6.5	6.4	6.3	6.4	6.3	6.2
West Germany	12.1	8.8	5.7	5.7	5.3	5.7	6.1	5.9	6.4	6.1	5.9	5.8	5.8	6.1
United Kingdom	13.8	12.2	10.1	11.0	10.1	9.7	9.4	9.2	9.3	9.4	9.3	8.9	8.8	9.3
France	15.3	14.6	12.4	12.7	12.4	12.3	12.3	12.4	12.2	12.2	12.4	12.5	12.5	12.2
Italy	20.0	20.0	18.0	19.1	17.9	17.5	17.5	17.5	17.8	17.8	17.4	17.3	17.4	16.8

Note.--The figure for a quarter is the average rate for the last week of the quarter.

Source: Statistics provided by Federal Reserve Board.

Effective exchange rates of the U.S. dollar, unadjusted and adjusted for inflation differential
(Index numbers, 1980-82 average=100; and percentage change from previous period)

Item	1981	1982	1983	1983 I	1983 II	1983 III	1983 IV	1984 I	1983 Dec.	1984 Jan.	1984 Feb.	1984 March	1984 April	1984 May
Unadjusted:														
Index number	99.5	109.8	114.2	110.9	113.0	116.3	116.4	117.2	118.0	119.1	117.3	115.3	116.7	119.5
Percentage change	9.7	10.4	4.0	-2.5	1.9	2.9	0.1	0.7	1.3	1.0	-1.5	-1.7	1.2	2.4
Adjusted:														
Index number	100.7	109.8	112.4	110.1	111.1	114.1	114.3	114.4	115.4	116.4	114.4	112.3	113.1	115.4
Percentage change	12.5	9.0	2.4	-3.6	0.9	2.7	0.2	0.1	1.0	0.9	-1.7	-1.8	0.7	2.0

Note.--The foreign-currency value of the U.S. dollar is a trade-weighted average in terms of the currencies of 15 other major nations. The inflation-adjusted measure shows the change in the dollar's value after adjusting for the inflation rates in the U.S. and in these other nations; thus a decline in this measure suggests an increase in U.S. price competitiveness.

Source: World Financial Markets, Morgan Guaranty Trust Company of New York.